

Michigan Department of Treasury

Revenue Technical Tax Training



Sales and Use Taxes **Exemptions and Deductions** **July 2002**



STATE OF MICHIGAN DEPARTMENT OF TREASURY Revenue Training Manual

Sales and Use Taxes Exemptions and Deductions

This manual was prepared as an instructional text to be used in conjunction with classroom training on Michigan's Sales and Use Taxes – Exemptions and Deductions. The purpose of the manual is to explain the various provisions of the Sales and Use Tax Acts, the Department's policies and practices in administering the Acts and the applicable Revenue Administrative Bulletins, Rules and Regulations. It is not intended as a statement of law, Department policy or any official position independent of existing law and the Department's official administrative statements.

Rules and Regulations, Revenue Administrative Bulletins and Letter Rulings referenced herein are the most recent versions available as of the date of printing. Users may need to update this manual in the future when law changes, court cases or corrections affect the substance of the Acts or when policies and procedures that affect the administration of the Acts are revised.

This manual is intended only for training purposes and does not take the place of the law. This manual may not be distributed to the public without the express permission of the State Treasurer. Questions about the content of this manual may be directed to the Constituent Education Division.

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INTRODUCTION

In general, sales and use tax exemptions are based on: 1) what the item is, 2) who purchases the item, and 3) how the item is used. Frequently, a qualifying exemption from tax will be based on a combination of 2 or more of the 3 basic exemption types.

Currently, there are over 100 distinct exemptions provided for in the sales and use tax statutes. Generally exemptions in one law are mirrored in the other, but there are instances when exemption is not provided for in both laws. The following manual highlights some of the more common exemptions and is not intended to be all-inclusive.

The industrial processing exemption is not included in this manual as there is a separate manual that deals specifically with the industrial processing exemption and its complexity.

It is the responsibility of all taxpayers to maintain adequate records and required exemption claims, certificates and documents.

NOTE: Always reference current tax law. Do not rely solely on this manual for current interpretation of tax law. This manual replaces any earlier versions.

AGRICULTURAL PRODUCTION

The General Sales and Use Tax Acts provide exemption on tangible personal property to persons engaged in a business enterprise for items used in:

- 1) Tilling, planting, caring for, or harvesting of the things of the soil, or
- 2) Breeding, raising or caring for livestock, poultry or horticultural products for further growth
- 3) Commercial Fishing

The agricultural producing exemption in the General Sales Tax Act also includes the following when used in the production of agricultural products as a business enterprise:

- 1) Agricultural land tile, which means fired, clay or perforated plastic tubing used as part of a subsurface drainage system for land or subsurface irrigation pipe
- 2) Portable grain bins designed to be disassembled without significant damage to their component parts
- 3) Fuel and equipment sold to dry grain

NOTE: The Use Tax Act contains the agricultural producing exemption for land tiles and portable grain bins but **does not exempt subsurface irrigation pipe or fuel and equipment used to dry grain.**

The sales and use tax exemption does **not** include:

- 1) Transfers of food, fuel, clothing, or any similar tangible personal property for personal living or human consumption
- 2) Tangible personal property permanently affixed and becoming a structural part of real estate

NOTE: Since the decision in *William Mueller & Sons, Inc. v Michigan Department Of Treasury*, June 3, 1991, *Michigan Court of Appeals*, Docket 120500, we extend the exemption to servicers who use their equipment for agricultural or horticultural growth.

Livestock handling equipment and horse equipment, other than a trailer, are usually exempt when purchased by a farmer who raises livestock for resale or who uses horses to till the soil. However, handling equipment sold to boarding ranches, riding stables or individuals not in compliance with the definition of agricultural producing are taxable.

Although the term "livestock" is not defined in the statute, it is generally used to include horses, cattle, sheep and other useful animals kept or raised on a farm or ranch. It can also include dogs, cats, birds, goldfish, etc. The exemption includes only livestock or the offspring of an animal being bred if the offspring are intended to be sold or intended to be used as work animals on a commercial farm. The owner of livestock producing offspring for resale is required to be licensed for sales tax.

The agricultural exemption would apply to the breeding of a horse for sale or farm work. For example, you may purchase a mare tax exempt to breed race horses for sale. When the offspring are sold, you must collect sales tax on the retail-selling price. However, the breeding of an animal whose offspring will be used for the enjoyment of its owner or any other non-commercial farm use would not be exempt from tax.

Based on the above two paragraphs, it will be necessary for a breeder to maintain records to substantiate property consumed in exempt activities versus property consumed in taxable activities.

Farmers who sell more than food to final consumers are required to be licensed and pay sales tax on their taxable sales. It is immaterial whether the retail sales are made at the place of production, a roadside stand, a market, from a vehicle, or elsewhere (R 205.51).

Exempt food for human consumption includes sales of live animals purchased with the intent to be slaughtered for human consumption.

Sales of the following are usually not subject to tax when used in agricultural production as a business enterprise:

- Seeds and other reproductive portions of plants (R 205.51)
- Fertilizer and similar substances for improving the quality of the soil (R 205.51)
- Spray materials for insecticides, germicides, and fungicides (R 205.51)
- Livestock, poultry, their feeds, and foodstuffs, including salt, bone meal, cod-liver oil, limestone, grit, oyster shell, and other similar substances used to sustain animals or poultry (R 205.51)
- Sacks, wrappers, and other nonreturnable containers resold with crops; also binding twine and baling wire (R 205.51)
- Machinery, tools, other equipment, repair parts, motor fuel, oil, grease, and other tangible personal property necessary for their operation and maintenance with the exceptions of licensed highway vehicles, maintenance of these licensed highway vehicles, and property attached to or becoming a part of real estate (R 205.51)
- Irrigation systems that remain personal property
- Greenhouses constructed by driving pipe into the ground and covering with a plastic framework. This is personal property, as it does not meet the “three prong test” to determine realty. See the “Contractor” section of this text.
- Electricity or gas used directly in producing agricultural products. When one meter measures both taxable and exempt usage, the farmer will have to substantiate the exempt portion. If the farmer’s total electrical consumption exceeds 1,500 kwh per month (or 2,500 kwh per month for a home with electric heat) during the period of November to March, the consumption in excess will be considered exempt if the farmer provides the seller with the approved agricultural producing exemption certificate. (R 205.115)
- The airplane, gas, oil, and parts used in crop-dusting airplanes licensed for restrictive use in agricultural service or fuel consumed in other equipment used for spraying crops
- Readily movable equipment such as portable hog houses and feeding troughs
- Land tile and portable grain bins purchased by a contractor for resale and installed, when a proper exemption is secured
- Subsurface irrigation pipe purchased in Michigan by a contractor for resale and installed, when a proper exemption is secured
- Boxes used to harvest fruit or vegetables. These containers usually have dual uses and are taxed on a percentage basis.
- Tractor blades used to scrape organic matter from the barn floor and feedlot area

- Grain drying equipment and natural and propane gas to fuel that equipment for agricultural purposes. This same kind of equipment and fuel may qualify for the industrial processing exemption, if the grain is owned by the industrial processor.
- Accessories sold as original equipment with tractors, such as heaters, two-way radios and air conditioners. Two-way radios sold separately would not qualify for the exemption, as they are not used to produce agricultural products. (LR 79-16)

The following sales are subject to tax because they do not qualify for the agricultural producing exemption as previously defined:

- Fuel, clothing, and all other personal property for personal living or human consumption
- Grass seed, fertilizers, equipment, and all other tangible personal property sold to individuals for use on lawns, non-commercial gardens, parks, boulevards, and golf courses or for use by landscape gardeners (R 205.51)
- Sales of tangible personal property used to construct, maintain, or repair barns, fences (other than portable fences), water supply systems, drains, and all other structures forming a part of real estate, other than qualifying subsurface irrigation pipe and land tile (R 205.51)
- Pea gravel, metal outlet pipe or culvert, if used in a subsurface drainage system even when the land tile or perforated tubing is exempt (RAB 91-11)
- Land tile used in the yard around the farm house (RAB 91-11)
- Free stalls bolted to barns to hold farm animals. Bolted is usually construed as a permanent attachment to realty. It does meet the "three prong test" to determine realty. See the "Contractor" section of this text.
- Computer controlled ventilation fans bolted to the barn
- Trucks with inseparable sprayer units sold to servicers who will use them in providing a spraying service to farmers. Vehicles including attachments are taxable if licensed for use on public highways.
- Boxes used to ship commercial production to the processor. This is shipping, harvesting has ceased and the agricultural processing exemption ends with harvesting.
- Tangible property used to construct a grain silo that will become part of real estate (RAB 90-2)
- Game animals, feed, supplies, etc. purchased by one who provides animals to be hunted. This business is considered to be a service.
- Prescription and nonprescription drugs, animal health products, dog food, feed additives, and supplies sold to veterinarians. Unless purchasing for resale, veterinarian purchases are taxable as they are providing a professional service. Their supplies will not become exempt, even if the veterinarian renders services to a cattle farmer. (RAB 90-24)
- Equipment used to measure temperatures to detect spoilage in a grain storage bin. Although the law exempts certain grain storage bins, storage after harvest does not fall into the scope of the exemption. Storage is not tilling, planting, caring for, harvesting or transferring for further growth. (LR 83-7)

- Subsurface irrigation pipe purchased outside of Michigan for use in Michigan. (If it is purchased in Michigan for use in Michigan, it is exempt.)

COMMERCIAL FISHING

The General Sales Tax Act exempts commercial fishing. **The Use Tax Act has no such exemption.** Purchases made from out-of-state sellers are not exempt. Also, lease arrangements where the lessor collects use tax on rental receipts are not exempt from tax.

To qualify for the exemption, the items purchased must be used only by an owner-operator of the business enterprise in the direct gathering of fish, by net, line, or otherwise, not including a charter fishing business enterprise.

There are individuals in the business of harvesting bait, etc. for sale to others. These businesses do not qualify for the commercial fishing exemption unless their catch is fish. The exemption is limited to items used in the direct gathering of fish.

Tangible personal property that may be purchased exempt from sales tax includes:

- Nets of all types
- Bottom stakes
- Hook lines
- Baits
- Winches
- Lines
- Ropes
- Commercial fishing boats
- Oil and fuel
- Fish and depth finders
- Buoys
- Markers
- Anchors
- Any safety equipment required by law to be on board
- Any other property used in the direct gathering of fish

The raising of fish on fish farms qualifies for the agricultural producing exemption and does not rely on the exemption established for commercial fishermen.

References: MCL 205.54a(1)(e)
MCL 205.54g(3)
R 205.51
R 205.115
RAB 90-2
RAB 90-24
RAB 91-11
LR 72-10
LR 79-16
LR 83-7
LR 85-16
LR 86-37

William Mueller & Sons, Inc. v Michigan Department of Treasury

AIRCRAFT/AIRCRAFT PARTS

The General Sales and Use Tax Acts provide exemption for certain aircraft.

The Sales Tax Act exempts sales to “domestic air carriers” of: (Effective 6/26/2000)

- Aircraft with a maximum certified takeoff weight of at least 6,000 pounds used solely in the transport of air cargo, passengers, or a combination of both.
- Parts and materials, excluding shop equipment or fuel, affixed or to be affixed to the above specified aircraft.

Use tax does not apply to the storage, use or consumption by a “domestic air carrier” of:

- An aircraft purchased after 12/31/92 but before 10/01/96 for use solely in the transport of air cargo that has a maximum certificated takeoff weight of at least 12,500 pounds.
- An aircraft purchased after 06/30/94 but before 10/01/96 that is used solely in the regular scheduled transport of passengers.
- An aircraft purchased after 12/31/94 but before 10/01/96 that has a maximum certificated takeoff weight of at least 12,500 pounds and that is designated to have a maximum passenger seating configuration of more than 30 seats and used solely in the transport of passengers.
- An aircraft stored, used or consumed by a domestic air carrier after 09/30/96 for use solely in the transport of air cargo and/or passengers, that has a certificated takeoff weight of at least 6,000 pounds.

Use tax does not apply to parts and materials, excluding shop equipment or fuel, affixed to or to be affixed to any of the aircraft previously described.

“Domestic Air Carrier” is defined in both acts as an entity primarily engaged in the commercial transport for hire of cargo and/or passengers as a business activity.

Effective 7/11/2001 both acts exempt aircraft for subsequent lease to a domestic air carrier operated under a certificate issued by the Federal Aviation Administration under 14 C.F.R. 121, for use solely in the regularly scheduled transport of passengers.

References: MCL 205.54x
 MCL 205.94 (u) through (y)
 MCL 205.94k

BAD DEBTS

A bad debt is that portion of an account receivable resulting from a sale that has become worthless. For federal income tax purposes, the worthless portion is allowed by the Internal Revenue Code (IRC) as a deduction from income. The deduction is computed based on a direct write-off method or the allowance method.

The **direct write-off method** identifies specific accounts that have become uncollectible. The deduction per the IRC takes place in the year the specific account has been determined to be uncollectible.

A calculation of “estimated” expected uncollectible accounts is known as the **allowance method of computing bad debts**. The estimate is based on experience and is not comprised of specific, identifiable uncollectible accounts receivable. The write-off generally takes place in the period that the sales on account are made.

For sales tax purposes, a bad debt is defined as that portion of a debt or account receivable relating to a taxable sale at retail, or to prepaid sales tax on gasoline which has become uncollectible. It must be eligible to be claimed as an IRC deduction. Furthermore, the debt or worthless account receivable must be identifiable. If an amount is deducted on the federal income tax return and the allowance method was used the deduction on the sales tax return is generally allowed only when **specific accounts are identified** and determined to be worthless.

Effective 07/14/99 bad debt deductions are allowed pursuant to the Use Tax Act, MCL 205.99a. The deduction is retroactive to 03/30/95. For use tax purposes a bad debt is defined as any portion of a debt resulting from a seller’s collection of the use tax on the purchase of tangible personal property or taxable services that has become worthless or uncollectible.

Records **must** be maintained to establish the validity of the deductions. These records include the following:

- Name of purchaser/debtor
- Date of sale(s) giving rise to the bad debt
- Price of the property and the amount of the sales or use tax charged
- Amount of interest, finance or service charges included in the debt or account
- Dates and amounts of any payments made on a debt or account
- Portion of the debt or account not subjected to tax in the original transaction

Should documentation not be maintained, the allowable maximum deduction shall be equal to the following:

$$\text{bad debt expense} \times \frac{\text{prior year taxable sales}}{\text{prior year total sales}}$$

Bad debt deductions **are limited to taxable transactions**; they **do not** include amounts for any of the following:

- Interest or finance charges
- Sales or use tax charged on the original sale
- Uncollectible amounts on property which remains in the possession of the seller until the full purchase price is paid, e.g., property placed on layaway
- Expenses incurred attempting to collect a bad debt, which is subsequently collected
- Any bad debt or account sold to a third party for collection with or without recourse
- Sales or use tax charged on property that is subsequently repossessed
- Bad debt claim made more than four years after tax was paid

Should a taxpayer subsequently collect all or a portion of an account previously written off as uncollectible, the collected portion should be reported as a taxable transaction **in the period** collected. In the event the deduction was based on the formula, then the percentage calculated by using the above formula would be applied to the **amount collected** and this would be reported as a taxable sale. If a wholesaler of gasoline later collects an amount for which a prepaid sales tax bad debt deduction was claimed, the tax collected is used to adjust the credit due to the wholesaler on the next Wholesale Gasoline Distribution Supplemental Sales Tax Report (form #429).

References: MCL 205.54i
MCL 205.99a
RAB 89-61

Michigan Bell Telephone Company v Michigan Department of Treasury,
229 Mich.App. 200 (1998), app. den. 459 Mich. 972

BROADCASTERS

Tax does not apply on tangible personal property sold to or purchased by persons licensed to operate commercial radio or television stations if the tangible personal property is used in the origination or integration of the various sources of program material for commercial radio or television transmission.

The exemption does not apply to vehicles for use on public roadways or to property used in the transmitting to or receiving from an artificial satellite.

Reference: MCL 205.54a(1)(g)
MCL 205.94(1)(m)
RAB 97-1

CHURCHES

The statute provides an exemption for churches to purchase items with **church funds** for **church use**. A purchase by an individual on behalf of the organization is taxable, even if the church later reimburses the individual.

Sales to religious organizations and societies composed of church members are taxable (e.g., men's club, women's guild, etc.). No exemption applies if members or others who join the group reimburse the church for participation in a tour or program (LR 81-4).

Sales of property used in a commercial enterprise by a church or a house of worship are taxable [MCL 205.54a(1)(b)]. For example:

A church has a weekly fish fry during Lent. They contract with a caterer, who prepares the food. A ticket is purchased at the door which covers the cost of the meal, as well as the cost of the church's overhead (lights, heat, etc.). This is considered a commercial enterprise transaction, and the church is required to register and obtain a sales tax license (RAB 91-19).

Vehicles licensed for use on the public highways, purchased by a church, are generally taxable. The exception is the purchase of a passenger van or bus that has a manufacturer's rated seating capacity of 10 or more and is used primarily for transporting people for religious purposes. Repairs, gas and maintenance on all church vehicles are exempt [MCL 205.54a(b)].

In the *Pioneer Construction Company v Michigan Department of Treasury*, Nov. 7, 1990, *Michigan Court of Appeals*, No. 118388 case, a church bought materials and a contractor affixed the materials to realty. The Court held the contractor liable for use tax, as Pioneer was the consumer of the materials. See the "Contractor" section of this text.

Recent amendments exempted from sales tax tangible personal property acquired by a contractor and affixed to or made a structural part of a sanctuary. As defined in the amendment, "sanctuary" means "only that portion of a building that is owned and occupied by a regularly organized church or house of religious worship that is used predominantly and regularly for public worship". The religious organization must be qualified under section 501(c)(3) of the Internal Revenue Code (IRC) of 1986. (PA 275 of 1998)

Retail sales made by a church are exempt from tax if aggregate sales at retail for the calendar year are less than \$5,000. Churches making retail sales are still required to register for a sales tax license even if their total sales are below the limit. If the total sales at retail are \$5,000 or greater, the tax is due on the entire amount. Sales tax billed separately must be remitted regardless of the \$5,000 exception. (PA 156 of 1994)

References: MCL 205.54a(1)(b)

MCL 205.94(i)

RAB 91-19

RAB 95-3

LR 81-4

Pioneer Construction Company v Michigan Department of Treasury

COINS AND BULLION

Effective July 7, 1999, neither sales nor use tax applies to the sale, purchase, storage, use, or consumption of investment coins and bullion.

Both acts define “bullion” as gold, silver, or platinum in a bulk state, where its value depends on its content rather than its form, with a purity of not less than 900 parts per 1,000.

The Acts also define “investment coins” as numismatic (collector) coins or other forms of money and legal tender manufactured of gold, silver, platinum, palladium (metallic element alloy mixed with gold, silver, etc.), or other metal and issued by the United States government or a foreign government with a fair market value greater than the face value of the coins.

References: MCL 205.54s
 MCL 205.94u

COMMERCIAL ADVERTISING

The statute states “Sale at retail” does not include a commercial advertising element when the use of the element meets **all** of the following:

- 1) The element is used to create or develop a print, radio, television, or other advertisement
- 2) The element is discarded or returned to the provider after the advertising message is completed
- 3) The element is custom developed by the provider for the purchaser [MCL 205.51(h)]

If all three qualifiers are not met, the property **may** be subject to sales tax and the real object test must be used if there is doubt as to whether the sale is of tangible personal property. Refer to

RAB 95-1 for detailed information on the “real object test”.

“Commercial advertising elements” are specifically defined in the statute as:

- A negative or positive photographic image
- An audio tape or videotape master
- A layout
- A manuscript
- Writing of copy
- A design
- Artwork
- An illustration
- Retouching
- Mechanical or keyline instructions

“Sale at retail” does include black and white or full color process separation elements, an audiotape reproduction or a videotape reproduction; therefore these items are taxable (MCL 205.92(1)).

The statute excludes commercial advertising elements from the definition of “tangible personal property” [MCL 205.92(1)].

References: MCL 205.51(h) MCL 205.92(1) RAB 95-1

COMMUNICATION SERVICE PROVIDERS

Certain **communication services** are taxed in the same manner as tangible personal property.

INTRASTATE (Within Michigan)

Taxable intrastate telephone, telegraph and leased wire communications include items such as the following:

- Telephone (land-line and cellular)
- Telegraph
- Leased wire
- Similar communications
- Long distance telephone service that both originates and terminates in Michigan
- Teletypewriter
- Private line
- Communication services by a reseller

Exempt intrastate telephone, telegraph, and leased wire communication includes:

- Coin operated service
- Switchboards
- Pager Service (one-way)
- Directory advertising proceeds
- Pass-through charges from a 3rd party service provider (e.g. roaming charge)

INTERSTATE (Between States)

Interstate telephone communications are generally taxable. This includes telephone communications that originate **or** terminate in this state if the charge for the service is billed to a Michigan service address or phone number.

The tax **does not** apply to the following services:

- Wide area telecommunication service (WATS lines) or similar services
- 800 or similar type prefix service (e.g. 888, 887)
- Interstate private network
- International telecommunication service

Sales of communication services to the following are exempt from tax:

- United States Government and its entities
- State of Michigan and its entities
- American Red Cross
- Nonprofit Schools
- Nonprofit Hospitals
- Nonprofit Homes for the Aged or Children
- Nonprofit Charitable Institutions

PURCHASES BY COMMUNICATION SERVICE PROVIDERS

Machinery and Equipment used in providing taxable communication services must meet either of the following to be exempt from tax:

- Be located on the premises of the subscriber
- Be central office equipment or wireless equipment directly used or consumed in transmitting, receiving, or switching 2-way interactive communication

Central office equipment or wireless equipment does not include distribution equipment including cable or wire facilities.

Effective April 1, 1999, there is an irrebuttable presumption that 90% of total use as defined in subsection 1 is for exempt purposes. This presumption is in effect until April 1, 2006, at which time the presumption shall be reviewed and redetermined by the department using nonexempt and exempt user information for the previous 12-month period. That redetermined irrebuttable presumption shall be in effect for the following 7 years. The irrebuttable presumption shall be reviewed and redetermined every 7 years after April 1, 2006 and applied to the following 7 years.

References: MCL 205.54v MCL 205.93a(a)(c)
MCL 205.94q R 205.110

MCI et. al. v Michigan Department of Treasury, Michigan Court of Appeals, July 15, 1997, Nos. 188378, 188422, 188483 (unpublished)

COMPUTER SOFTWARE (CUSTOM)

The following computer software charges are exempt from sales and use tax:

- Charges for technical support if optional and separately stated
- Charges for modifying canned software to a purchaser's needs **if** the charges are separately stated and identified
- Computer software originally designed for the exclusive use and special needs of the purchaser

References: MCL 205.51(1)(e)
 MCL 205.92(f)
 MCL 205.92(k)
 RAB 99-5

CONTRACTORS

Contractors are defined as persons engaged in the business of constructing, altering, repairing, or improving real estate for others to the extent the tangible personal property is affixed to and made a structural part of the real estate. Contractors are consumers and therefore, sales to contractors are retail sales.

AFFIXATION TO REALTY

Construction contractors consume tangible personal property by affixing it to and making it a structural part of real estate. The various Michigan courts are collectively in agreement that an affixation to realty **must** meet three tests:

- Be attached to realty
- Its function must benefit the realty
- It is intended to be a permanent part of realty

Generally, if property depends on the building utilities for operation and use, and is connected to the building utilities (gas, electric, plumbing etc.), it would be deemed to be affixed to realty.

Definitions and Important Terms Relating to Contractors

Use - MCL 205.92(b)

An exercise of a right or power over tangible personal property incident to the ownership of that property including transfer of the property in a transaction where possession is given.

Acquire

This term is not defined in the Sales or Use Tax Acts. The Michigan Court of Appeals decision in *Pioneer Construction Company v Michigan Department of Treasury*, Nov. 7, 1990, *Michigan Court of Appeals*, No. 118388 determined that acquired was not equivalent to ownership. This definition was crucial to the case.

Pioneer Construction Company entered into a contract with a church to construct new additions to the existing church structure. The church purchased the materials independent of Pioneer Construction Company who was to construct the additions, providing labor only. The church purchased materials tax exempt pursuant to the Sales Tax Act. The department held Pioneer Construction Company liable for use tax on the cost of the materials.

The Appeals Court accepted the definition of “acquire” in Webster’s Third New International Dictionary - “to come into possession, control, or power of disposal often by some uncertain or unspecified means...” Consequently, the court accepted the state’s argument that Pioneer Construction Company exerted possession and control over the materials. They had in fact acquired the material and were responsible for the tax.

Purchase - MCL 205.92.(e)

Purchase means to acquire for a consideration, whether the acquisition is effected by a transfer of title, of possession, or of both, or a license to use or consume; whether the transfer is absolute or conditional, and by whatever means the transfer is effected; and whether consideration is a price or rental in money, or by way of exchange or barter.

Realty/Real Estate

Real estate is defined as land, including the buildings or improvements on it and its natural assets, as minerals, water, etc. Realty has the same meaning as real estate.

For tax purposes RAB 88-35 makes specific mention of a Michigan Supreme Court decision in Sequist v Fabiano, 274 Mich. 643; 265 NW 488 (1936). In this case, the court applied a “three prong test” to determine realty:

- 1) Annexation (to join, connect) to realty, either actual or constructive
- 2) Adaptation or application to the use or purpose to which that part of the realty to which it is connected is suitable
- 3) Intention to make the article a permanent accession (addition) to the freehold (an estate in land)

Section 205.92(f) - Price

Price means the aggregate value in money of anything paid or delivered, or promised to be paid or delivered, by a consumer to a seller in the consummation and complete performance of the transaction by which tangible personal property or services are purchased or rented for storage, use, or other consumption in this state. Deductions are not allowed for the cost of the property sold, cost of materials used, labor or service cost, interest or discount paid or any other expense.

The price of tangible personal property, for affixation to real estate, withdrawn by a construction contractor from inventory available for sale to others or made available by publication or price list as a finished product for sale to others is the finished goods inventory value of the property.

Section 205.92(g) - Consumer

Consumer means the person who has purchased tangible personal property or service for storage, use, or other consumption in this state and includes a person acquiring tangible personal property if engaged in the business of constructing, altering, repairing, or improving the real estate of others.

EXEMPTIONS

Prior to a 1970 amendment to the use tax act the exemption for affixations to realty extended to the U.S. Government, Michigan and its political subdivisions, churches, schools, and nonprofit organizations. The legislature specifically limited the exemption for contracts in the 1970 amendment to nonprofit hospitals and nonprofit housing. Subsequently exemptions have been extended to the construction of sanctuaries and, under certain restrictions, to qualified business activity (Enterprise Zones).

The sales and use tax acts contain a rare flow through exemption to real property contractors for tangible personal property they acquire and affix to and make a structural part of real estate of a nonprofit hospital and nonprofit housing.

This section will cover types of contractors and statutory provisions exempting tangible personal property affixed to realty.

1. Contractors
2. Manufacturer/Contractors
3. Construction of nonprofit hospital
4. Construction of nonprofit housing
5. Construction of a Sanctuary
6. Construction in the Enterprise Zone
7. Construction of Pollution Control Facilities

1. Contractors (Administrative Rule 205.71)

- 1) Contractor includes only prime, general, and subcontractors directly engaged in the business of constructing, altering, repairing or improving real estate for others.
- 2) Contractors are consumers of the materials used by them. All sales to or purchases by contractors of tangible personal property are taxable, except when affixed and made a structural part of real estate for a qualified exempt nonprofit hospital or a nonprofit housing entity qualified as exempt under the Sales and Use Tax Acts. All materials consumed in the performance of such contracts and not affixed and made a structural part of real property are taxable. Retailers making exempt sales shall obtain a valid exemption certificate.
- 3) Sales and rentals of tools, machinery and equipment to contractors are taxable.
- 4) Where a contractor is exclusively engaged in the contracting business and makes no direct sales to other contractors or consumers, he does not need a sales tax license. Such non-licensed contractors are required to maintain a use tax registration and pay the state on purchases made from out-of-state sellers.
- 5) Where a contractor is not exclusively engaged in the contracting business but makes sales of tangible property at retail to other contractors and consumers, he shall secure a sales tax license and file returns to report sales on such transactions. Use tax due on out-of-state purchases and on merchandise acquired for resale and later consumed in contract operations shall be reported on the combined sales and use tax returns.
- 6) A contractor purchasing tangible personal property for affixation to realty where delivery is taken in Michigan is subject to sales or use tax on the purchase price. It makes no difference whether the improvement or construction of realty takes place within or without Michigan, except in cases of exemption.

Tax Base for Contractors

Price as defined earlier will be different depending on the particular situation. The following examples will act as illustrations:

- 1) Contractor does not have a sales tax license; sales tax is paid to the vendor and is based on the vendor's selling price.
- 2) Contractor does have a sales tax license; use tax is paid at the time the contractor removes the tangible personal property from inventory for affixation to realty. The tax base is cost.

2. Manufacturer/Contractor [Section 205.92(f)]

If a construction contractor manufactures, fabricates, or assembles tangible personal property before affixing it to real estate, the tax base is determined by whether or not the contractor maintains an inventory available for sale to others or makes tangible personal property available to others through publications or price lists.

“Manufacture” means to convert or condition tangible personal property by changing the form, composition, quality, combination, or character of the property. “Fabricate” means to modify or prepare tangible personal property for affixation or assembly.

Tax Base for Manufacturer/Contractor

Determining the tax base for the manufacturer/contractor when the tangible personal property to be affixed to realty is:

1. Available for sale to others (Price List or Publication)
2. Not available for sale to others

Available for sale to others (Publication or Price List)

The material cost of property withdrawn by a construction contractor from inventory available for sale to others or made available by **publication** or **price list** as a finished product for sale to others is the finished goods inventory value of the property.

Publications - MCL 205.92(f)

Publications are not defined in the statute. The Department defines publications as printed material, the purpose of which is to offer tangible personal property for sale to others. Printed material includes catalogs, sales pamphlets, sales handbills, etc.

- Catalog - bound, stitched, sewed, or stapled book or pamphlet, containing a list and description of goods, wares, or merchandise with specific information, with or without a price.
- Sales Pamphlet - printed work concerning goods, wares, or merchandise. It consists of more than one sheet of paper that is stapled, sewed or stitched, with or without prices.
- Sales Handbill - it is often referred to as a “circular” or “dodger”. It is a single piece of paper intended to be circulated and concerns goods, wares, or merchandise.

Price List - MCL 205.92(f)

The statute does not define “price list”. It is generally accepted that the purpose of a price list is to offer tangible personal property for sale to others. The Department defines price list as a numerical or alphabetical enumeration of goods, wares, or merchandise items, quoting wholesale and/or retail prices and printed cards or sheets of paper, presented in loose-leaf form, stapled, stitched, or bound, or available on computer database, disk, or tape.

The use tax base for tangible personal property made available through inventory, publications and/or price lists: is finished goods inventory value of the property. This value is defined in MCL 205.92(f), and MSA 7.555 (2)(f). The definition in each document is basically the same, “all direct production costs” which are

to include components of direct materials, direct labor, and indirect production costs. The indirect production costs are generally included to the extent they are incidental to and necessary for manufacturing operations.

Components of Finished Goods Inventory Value

1) Direct Materials

- Raw materials (including freight in)
- Amounts paid for processing by a second party
- Supplies entering into production
- Supplies consumed in connection with the product

2) Direct Labor:

- Basic wages
- Overtime wages
- Sick leave pay
- Vacation and holiday pay
- Shift differential
- Payroll taxes
- Payments to a supplemental unemployment benefit plan
- Any other payments incurred on behalf of employees directly engaged in production

3) Indirect Production Costs:

- Repairs and maintenance costs
- Utility costs
- Rents and taxes on buildings and machinery necessary for production
- Indirect labor and production supervisory wages (components are same as outlined in direct labor)
- Miscellaneous indirect costs including:
 - a) Indirect materials and supplies
 - b) Expensed tools and equipment
 - c) Costs of quality control and inspection
 - d) Depreciation and depletion incident to production or manufacturing operations or processes.
 - e) Employee benefits
 - f) Costs attributable to strikes
 - g) Rework labor
 - h) Scrap and spoilage
 - i) Administrative costs of production
 - j) Officers' salaries incident to production
 - k) Insurance costs incident to production

Not available for sale to others

When a manufacturer/contractor does not make tangible personal property available for sale to others, through inventory, publications and/or price lists, the use tax base is equal to the sum of material cost and cost of labor to manufacture, fabricate, or assemble the property.

Tax base does **not** include the cost of labor to cut, bend, assemble or attach property at the site of affixation to real estate. The cost of labor to transport the product to the job site is specifically excluded from the tax base.

3. Construction of Nonprofit Hospital

Sales Tax Act Section 205.54w

Tangible personal property sold to a person directly engaged in the business of constructing, altering, repairing, or improving real estate for others is exempt to the extent that the property is affixed to and made a structural part of a nonprofit hospital.

An exemption will not be granted under this section for any portion of property otherwise qualifying for exemption under this section if income or a benefit inures directly or indirectly to an individual, private stockholder, or other private person from the independent or nonessential operation of that portion of property.

As used in this section: Nonprofit hospital” means 1 of the following:

1. That portion of a building to which 1 of the following applies:
 - Is owned or operated by an entity exempt under section 501(c)(3) of the internal revenue code of 1986 that is licensed as a hospital under part 215 of the Public Health Code,
 - Is owned or operated by a governmental unit in which medical attention is provided.
 - Is owned or operated by an entity or entities exempt under section 501(c)(2) or (3) of the internal revenue code of 1986 in which medical attention is provided.
2. That portion of real property necessary and related to a building in which medical attention is provided.
3. A county long-term medical care facility built after December 31, 1995.

“Nonprofit hospital” does **not** include the following:

1. A freestanding building or other real property of a nursing home or skilled nursing facility licensed under Part 217 of the Public Health Code
2. A hospice licensed under Part 214 of the Public Health Code
3. A home for the aged licensed under Part 213 of the Public Health Code

“Medical attention” means that level of medical care in which a physician provides acute care or active treatment of medical, surgical, obstetrical, psychiatric, chronic, or rehabilitative conditions, that require the observation, diagnosis, and daily treatment by a physician.

Use Tax Act Section 205.94s

Exempts property used in certain improvements to real estate including property purchased by a person engaged in the business of constructing,

altering, repairing, or improving real estate for others to the extent the property is affixed to and made a structural part of the real estate of a nonprofit hospital. A nonprofit hospital includes only that portion of the property of a nonprofit hospital the income or property of which does not directly or indirectly inure to the benefit of an individual, private stockholder, or other private person.

See above for definitions relating to “nonprofit hospital” and “Medical attention”.

Tangible personal property acquired by contractors for affixation to the realty of a nonprofit hospital is exempt from tax. Effective July 1, 1999 the Sales Tax and Use Tax Acts were amended. The amendments redefined a nonprofit hospital and allows the exemption to be calculated on a pro rata basis. Two tests have been provided to establish the validity of the claimed exemption. The nonprofit hospital must:

- Meet the statutory definition provided at MCL 205.94s(3) and
- Meet the inurement test at MCL 205.94s(2).

The Acts provide 3 separate definitions of what a nonprofit hospital has to be in order to be exempt from taxation. The exemption will be granted under the statute if any one of the definitions is met.

A building owned by a hospital and passing the inurement test would qualify for exemption. This would be true even if the hospital operated a commercial venture in the building. In instances where a single building is being constructed and will have multiple uses, some of which will not pass the inurement of benefit test, only that portion not meeting the test will be taxable. Examples of this would be the construction of a building a portion of which would be used as follows:

- Office space in a nonprofit hospital is rented to physicians who will use the same space for their private practice. This portion is taxable and the remainder of the building could be exempt.
- Space is rented to persons to conduct commercial activities:
 - Pharmacy
 - Gift shop
 - Coffee shop
 - News stand
 - Medical apparatus outlet
 - Cafeteria

Generally, all real estate owned by a hospital entity will qualify for the contractor flow through exemption. This will include such items as parking lots and structures, whether or not connected to or near the building in which medical attention and nursing are given. This will also include the “guest house” buildings.

Sales Tax Act Section 205.54z

Exemption for taxes levied after December 31, 1990 and before July 1, 1999 on tangible personal property used in the construction, alteration, repair, or improvement to nonprofit hospitals. provided a claim for exemption was made and it met the following criteria:

- 1) Contract must be binding and entered into prior to July 1, 1999
- 2) The claimed exemption was made in good faith
- 3) The entity making the claim must meet the definition of a nonprofit entity

Use Tax Act Section 205.94v

Exempts contracts entered into with nonprofit hospitals for the period January 1, 1991 through June 30, 1999 provided a claim for exemption was made and it met the following criteria:

- 1) Contract must be binding and entered into prior to July 1, 1999
- 2) The claimed exemption was made in good faith
- 3) The entity making the claim must meet the definition of a nonprofit entity provided at MCL 205.94s(3)(a)(i).

4. Construction of Nonprofit Housing

Tangible personal property sold to a person directly engaged in the business of constructing, altering, repairing, or improving real estate for others is exempt to the extent that the property is affixed to and made a structural part of a nonprofit housing entity qualified as exempt under Section 15a of the State Housing Development Authority Act of 1966.

Use Tax Act Section 205.94s

Property used in certain improvements to real estate is exempt including property purchased by a person engaged in the business of constructing, altering, repairing, or improving real estate for others to the extent the property is affixed to and made a structural part of the real estate of a nonprofit housing entity qualified as exempt pursuant to section 15a of the state Housing Development Authority Act of 1966, Act No. 346 of Public Acts of 1966, being section 125.1415a of the Michigan Compiled Laws. Nonprofit housing includes only that portion of the property of the homes or dwelling places constructed by a nonprofit housing entity, the income or property of which does not directly or indirectly inure to the benefit of an individual, private stockholder, or other private person.”

A nonprofit housing entity must be qualified as exempt pursuant to the state Housing Development Authority Act of 1966 (MSHDAA). Government housing projects are generally not in compliance with MSHDAA, thus they are taxable. Should the inurement test not be met, then that portion of the property otherwise qualifying for exemption would be taxed.

Shortly after the 1970 amendment, various entities that had lost their exempt status tried to avoid paying tax on contracts by purchasing the building materials with exempt funds and contracting separately with a contractor for the erection.

In November 1990, the Michigan Court of Appeals in *Pioneer Construction Co. v Michigan Department of Treasury*, Michigan Court of Appeal Docket No. 118388, November 7, 1990, ruled that contractors only have to “acquire” tangible personal property to be subject to use tax. **“Acquire” was determined not to be equivalent to ownership.** Consequently, when the church purchased building materials tax free for an

addition to the church, the contractor, Pioneer Construction Co. was deemed to have “acquired” it, that is, they exercised control over it. Thus, they were subject to tax since contractors are consumers.

5. Construction of a Sanctuary

Use Tax Act Section 205.94m and Sales Tax Act Section 205.54p

Tangible personal property acquired by a contractor for affixation to the “sanctuary” portion of a regularly organized church or house of religious worship is exempt from taxation. As used in this section, a sanctuary is limited to only that portion of a building that is:

- Owned and occupied by a regularly organized church or house of religious worship (must qualify under Section 501(c)(3) of the IRC of 1986.
- Predominately and regularly used for public worship.

6. Construction in the Enterprise Zone

Use Tax Act Section 205.94h

Tangible real or personal property is exempt for use in a qualified business activity of the purchaser. As used in this section, “qualified business activity” means activity as defined in the Enterprise Zone (EZ) Act. See the “Renaissance and Enterprise Zones” section of this text.

Qualified Business Activity

The exemption applies to persons who have been certified as a qualified business within the Enterprise Zone, acting as construction contractors who are directly engaged in the business of affixing to realty for others. The exemption will not apply if the construction contractor is not a qualified business and/or the affixation to realty is not within the Enterprise Zone boundaries. See the “Renaissance and Enterprise Zones” section of this text. The only enterprise zone in Michigan is in Benton Harbor.

7. Construction of Pollution Control Facilities

Tax does not apply to material purchases of tangible personal property which are specified on a proper tax exemption certificate issued by the State Tax Commission. See the “Pollution Control Facilities” section of this text.

OTHER STATUTORY REFERENCES

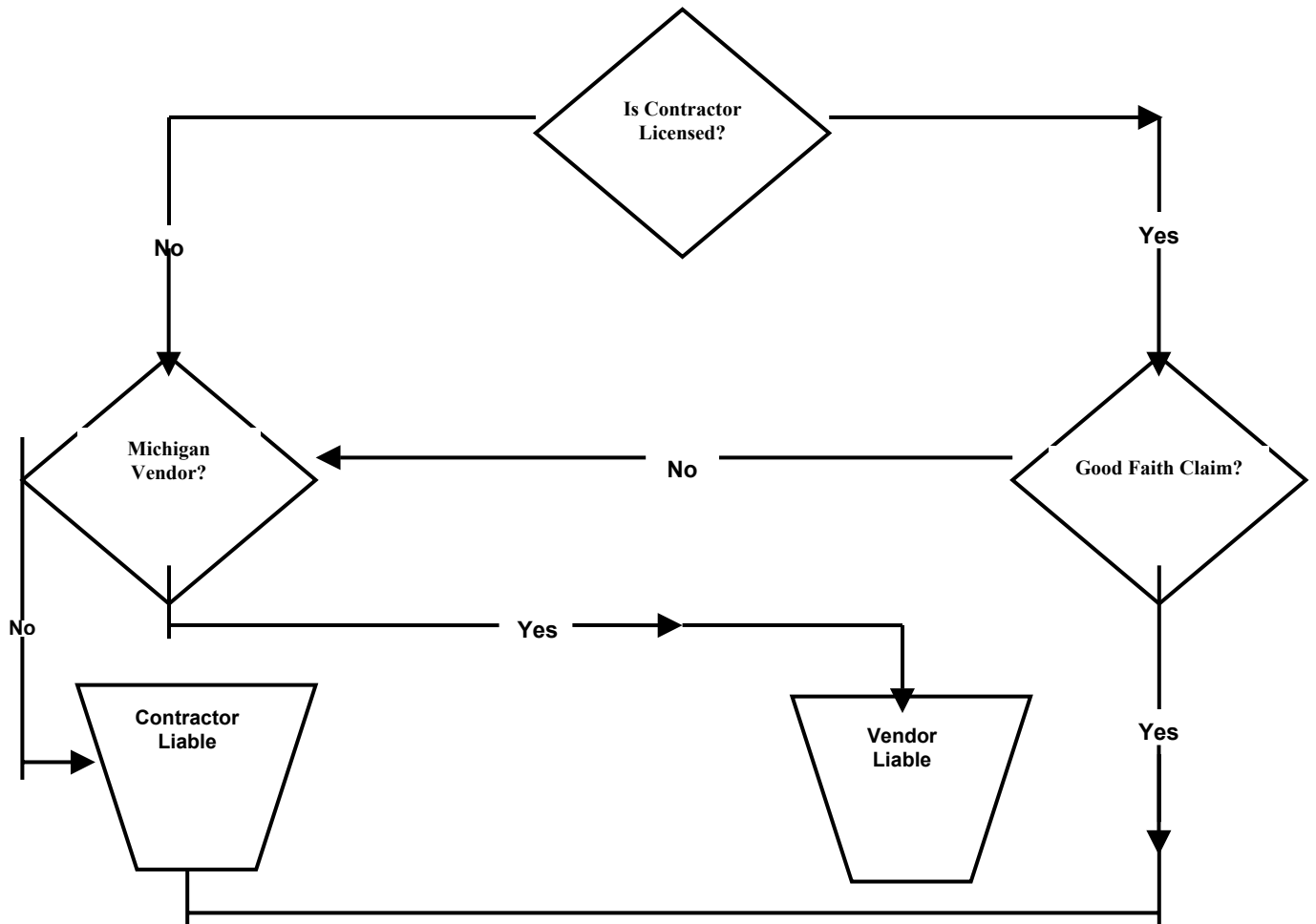
Sales Tax Statutory References

The Sales Tax Act makes an implied reference to contractors at MCL 205.51(1)(b), which defines sales at retail as sales of tangible personal property for consumption or use. [MCL 205.92(g)]

There are additional references in the Sales Tax Act that exempt contractors from taxation. The exemptions are based on when the contract was executed, or whom the contract was with. (Section 205.54m[1] Section 205.54c)

Flow Chart Of Who Is Liable For Tax - Contractor/Vendor

**Use Tax
Property Attached To Realty**
(ex: Nonprofit Hospitals/Housing and Sanctuary)



References:	MCL 205.54c	RAB 88-35	LR 70-5
	MCL 205.54m(1)	RAB 93-05	LR 74-05
	MCL 205.54p	RAB 93-10	LR 88-13
	MCL 205.54w	RAB 94-03	LR 89-63
	MCL 205.54z	RAB 99-2	LR 89-71
	MCL 205.92(e)		LR 90-24
	MCL 205.92(f)		
	MCL 205.92(g)		
	MCL 205.94(e)		
	MCL 205.94h		
	MCL 205.94m		
	MCL 205.94s		
	MCL 205.94v		

Pioneer Construction v Mi. Dept. of Treasury
Sequist v Fabiano

DROP SHIPMENTS

A drop shipment (or third party sale) is a transaction where an out-of-state retailer accepts an order from a Michigan consumer. The out-of-state retailer then places this order with a Michigan wholesaler. The out-of-state retailer directs the Michigan wholesaler to ship the property directly to the Michigan consumer.

To be a drop shipment, all of the following **must be true**:

- 1) Wholesaler or manufacturer is located in Michigan
- 2) The retailer must be located out of the state of Michigan
- 3) The consumer must be located in Michigan

Michigan wholesalers are not liable for Michigan sales tax on drop shipments **if** they submit a list to the Michigan Department of Treasury on an annual basis of all Michigan “drop shipments”. The list should include **all** of the following for both the Michigan purchaser and the out-of-state retailer:

- Name
- Address
- Federal ID Number (if available)

The Michigan purchaser **is liable for use tax** on the **purchase price** of tangible personal property, **unless** the tangible personal property was previously taxed or exempted by the Use Tax Act.

References: MCL 205.54k
MCL 205.94i
RAB 02-10

EXEMPTIONS AND REQUIREMENTS

CLAIM FOR EXEMPTION FROM TAX

A claim for exemption from sales tax is a **purchaser's statement to the seller stating that there is a reason for which tax should not be charged on the sale of tangible personal property or taxable services**. This claim is achieved by the purchaser providing a document that tells the seller that the item(s) being purchased is(are) exempt from the sales tax.

VARIOUS STATUTORY EXEMPTIONS

The more common exemptions allowed by the General Sales and Use Tax Acts are as follows:

- Sales for resale
- Sales to agricultural producers
- Sales to industrial processors
- Sales to governmental entities
- Sales not for resale to nonprofit schools, nonprofit hospitals, and churches
- Sales not for resale to other nonprofit organizations
- Catered meals purchased by exempt entities when not for resale
- Commercial fishing
- Materials consumed in contracts and made a structural part of the real estate of a nonprofit hospital or nonprofit housing, or church sanctuary

DOCUMENTATION NEEDED TO SUPPORT AN EXEMPTION

If exemption is claimed, a record shall be kept of:

- The name and address of the person to whom the sale is made
- The date of the sale
- The article purchased
- The use to be made of the article
- The amount of the sale
- The sales tax license number, if applicable

ACCEPTABLE EXEMPTION CLAIMS

- The prescribed claim form 3372
- Any exemption certificate found in a Sales and Use Tax Administrative Rule

- The Uniform Sales and Use Tax Exemption Certificate approved by the Multistate Tax Commission
- A purchase order issued by the purchaser

BLANKET PURCHASE EXEMPTION FORM

- Renewed every 4 years
- Lesser period if agreed upon by the seller and the purchaser
- Accepted in good faith
- Will be superseded by conflicting purchase order for that particular purchase only

The seller shall secure from the buyer a certificate or other approved documents that the sales are eligible for exemption. This relieves the seller from tax liability if it is established that the claim is invalid. An exemption claim must be presented by the customer for each exempt purchase, unless a blanket claim form is completed. The exemption claim must contain the signature of an authorized purchaser.

TAX EXEMPTION NUMBERS

The Michigan Department of Treasury does not issue tax exemption numbers. Sellers should not accept a “number” as evidence of exemption from sales and use taxes. A sales tax license number may support a tax exemption claim based on resale, but should not be the only evidence of exemption.

CLAIMS ACCEPTED IN GOOD FAITH

According to the statute as amended “**good faith**” means that the taxpayer received a completed and signed exemption certificate from the purchaser.

NOTE: The specific exemption requirements at MCL 205.54q requiring a copy of the nonprofit exemption letter supercedes the general exemption requirement at MCL 205.67.

References: MCL 205.67
MCL 205.104
RAB 96-6
Form 3372

FEDERAL PREEMPTION

The General Sales and Use Tax Acts grant exemption to the following:

- Sales to the United States Government
- Sales to its unincorporated agencies and instrumentalities
- Sales to any incorporated agency or instrumentality which is directly or indirectly owned by the United States
- Sales to the American Red Cross and its chapters and branches

PURCHASES BY FEDERAL GOVERNMENT AGENCIES:

Sales to and purchases by the United States government are not taxable if such sales are ordered on the prescribed government forms with payment made directly to the seller by warrants on government funds.

Since 12/1/98, credit cards used by federal employees to pay for products or services are referred to as SmartPay cards. There are four types of federal credit cards: purchase, fleet, travel and integrated.

Purchase and fleet cards can only be used to purchase items at certain establishments such as gas stations and office supply stores. Acquisitions using these cards are exempt from Michigan's taxes because they are billed direct to the federal government.

Travel and integrated cards are for official travel and are used at hotels, restaurants and similar establishments. Purchases using one of these cards can be taxable (billed to the employee) while another card's purchases can be exempt (billed direct to the government). Taxability depends upon the numbers on the card. A card billed to the individual (taxable) will

- Start with 4486, 4716 or 5568 and have a sixth digit that is either 1, 2, 3, or 4; or
- Have an account number that begins with 5568-16 from the Department of the Interior, the traveler does not carry an I.D. from the Bureau of Reclamation, and the purchase is for lodging or food.

The above categories of SmartPay cards are different colors with different graphics. They can say "For Official Government Travel" or "For Official Government Purchases Only" but, to be taxable, they must have the billing digits mentioned above. All other SmartPay cards with the other numbers are centrally billed and are exempt from Michigan's taxes.

Included in the definition of a federal instrumentality are federal credit unions and federal home loan banks. The federal credit union exemption is unique because it was granted by the court in the decision of *U.S. v State of Michigan, 1988, Sixth Circuit United States Court of Appeals, 851 F.2d 803*. The Court of Appeals decision stated that the incidence of the Michigan sales tax falls upon federal credit unions as purchasers rather than upon the retailer selling to them. Therefore, federal credit unions, which are exempt from direct state taxation by federal law, are not subject to sales tax on their purchases of tangible personal property for their own use. This exemption does not extend to national banks or federally chartered savings and loan institutions.

SALES BY FEDERAL GOVERNMENT AGENCIES:

Sales made by federal credit unions and federal home loan banks are subject to tax. This includes sales of checks or drafts to their customers. If checks were provided and a "service charge" was assessed, a sale was made.

Sales by the United States Post Office of uncanceled United States postage stamps, stamp books, envelopes, packaging materials, video tapes, neckties, etc. are handled differently from sales made by federal credit unions or by private entrepreneurs making sales on federal land. These sales are not being taxed by the United States Post Office.

The reason that tax is not being charged on the above sales is that the Federal government is claiming "federal preemption" (states may not impose a tax on the Federal government). Michigan's sales tax is statutorily imposed on the seller for the privilege of making sales at retail in Michigan. Thus, Michigan tax cannot be imposed on the Federal government.

SALES BY PRIVATE ENTREPRENEURS FROM FEDERAL AREAS:

Tax applies on sales made by private entrepreneurs who sell their wares on federal property, if the sale is not made directly to an exempt entity, including federal instrumentalities and nonprofit organizations. An example of this would be a privately operated concession stand at a national park.

References: MCL 205.54(7)
MCL 205.94(1)(g)
R 205.79
RAB 89-64
LR 90-24

U.S. v State of Michigan

FOOD FOR HUMAN CONSUMPTION

The Michigan Department of Treasury uses the following definition for food: “a nutritive material absorbed or taken into the body or an organism which serves for purposes of growth, work or repair and for the maintenance of the vital processes.”

The Sales Tax Act exempts "...food for human consumption, except prepared food intended for immediate consumption." The Use Tax Act also specifically exempts food for human consumption.

The following items are generally taxable:

- Alcoholic products of 1/2 of 1% or more alcohol content by volume, such as beer, wine and liquor
- Tobacco and tobacco products
- Prepared food for immediate consumption. This is all prepared food and drink sold by any type of restaurant, coffee shop or similar establishment.
- Prepared food for immediate consumption sold by exempt organizations such as churches or benevolent groups. This includes fund-raising projects. These organizations should have a sales tax license for the purpose of reporting sales and any tax due.

- Sales of prepared food and drink by a caterer
- Sales of prepared food cooked to order, or maintained at a temperature higher than room temperature

The following items are generally exempt:

- Bottled water intended primarily for human consumption
- Live animals purchased with the intent to be slaughtered for human consumption
- Retail sales of food for human consumption, normally considered as grocery items for home consumption
- Retail sales of plants that produce fruit or vegetables if sold by a business authorized to accept food stamps by the U.S. Dept. of Agriculture or a business that has made a complete and proper application for authorization to accept food stamps but has been denied authorization
- Dietary supplements including vitamins and herbs

RAB 91-18 provides a general taxable guide:

	ITEM	TAXABLE	EXEMPT
1.	Items sold at concessions	Taxable	
2.	Bakery items consumed on premise	Taxable	
3.	Food bars, such as soup and salad bars	Taxable	
4.	Deli trays	Taxable	
5.	Deli items that are sold at a temperature higher than room temperature (e.g. chicken, ribs)	Taxable	
6.	Sandwiches	Taxable	
7.	Prepackaged food items sold by carry-out restaurants	Taxable	
8.	Food sold and heated in convenience stores	Taxable	
9.	Popcorn and nuts in unsealed containers	Taxable	
10.	Food and nonfood combinations when the nonfood portion has a higher value	Taxable	
11.	Food stamp purchases		Exempt
12.	Bakery items consumed off premises		Exempt
13.	Deli items colder than room temperature sold by weight or measure (e.g. potato salad, sliced meat, cole slaw)		Exempt
14.	Frozen foods, including frozen sandwiches for on premise consumption		Exempt
15.	Sealed containers of beverages		Exempt
16.	Popcorn and nuts, presealed (e.g. heat-sealed or twist-tied)		Exempt
17.	Food and nonfood combinations when the food has a higher value		Exempt

MEALS PROVIDED BY SCHOOLS AND QUALIFIED EXEMPT NONPROFIT ORGANIZATIONS

Sales by a qualified exempt nonprofit organizations are not exempt simply because of the nonprofit status of the organization.

The following are examples of taxable food or meals:

- Food provided by a nonprofit organization at an event where an admission fee is required or a donation is made
- Meals sold by schools to nonstudents, including teachers
- Meals or direct sales from the caterer to the students

The following are examples of exempt food or meals:

- Meals provided to nonprofit groups, where the group pays for the meals, not the individuals attending
- Snacks such as coffee, juice or donuts, provided by nonprofit groups as part of a conference with no extra charge to persons attending
- Meals sold by schools to students duly enrolled in a program of that school

CATERED MEALS

All meals sold by caterers are subject to sales tax, except those sold to qualified exempt entities as “not for resale”. “Not for resale” means that the catered meals are paid directly from the exempt entity’s funds, with no reimbursement from the individuals attending the event. When a company pays a subsidy to the caterer, this amount is not included in gross receipts.

An example of an EXEMPT CATERED MEAL:

- The United Way sponsors a dinner for individuals that worked on the previous year's campaign. The dinner is paid for from United Way funds with no reimbursement from the individuals attending.

An example of a TAXABLE CATERED MEAL:

- The United Way hosts a dinner for business owners to encourage them to donate to the current year’s campaign. The business owners are required to purchase a ticket in order to attend the dinner

An example of a third party TAXABLE CATERED MEAL:

- A catering company provides food service to a university. The food service is exempt from tax for the meals provided by the university to the enrolled students. An association within the university contracts with the university to have a banquet in the university’s ballroom. This is a taxable event. The university would provide the catering company with a resale exemption certificate, then charge the association the appropriate taxes due.

An example of a third party EXEMPT CATERED MEAL:

- Assume the same facts as above, with one difference. The association provides the university with a proper claim for exemption as a non-profit organization, plus a copy of its exempt letter from the IRS as a designated 501(c)(3) or (4) entity.

The tax base for food and drink items included in a mandatory lump sum donation is the gross proceeds.

The sale of alcoholic beverages at a fund-raiser is taxable. Sales tax is due on the total amount of the sales of beer, wine and liquor. If an organization pays sales tax on alcoholic beverages when purchased and provides the alcoholic beverages at the fund-raiser at no additional charge to attendees, then no additional sales tax is owed. If at the fund-raiser there is a charge for alcoholic beverages, sales tax is due on the total gross proceeds of the beverage sales (a credit may be taken for any sales tax paid when the organization purchased the alcoholic beverages).

Sale of food or beverage at public events:

Prepackaged items (such as candy bars, potato chips, ice cream, popcorn, nuts or cans or bottles of soda) sold at various public events, facilities and places including theaters, fairs, recreation centers, athletic events, parks, and other similar public events, facilities or places, are taxable as prepared food for immediate consumption.

EMPLOYEE MEALS

Prior to October 1, 2001:

- Employee meals fall under the Sales Tax Act, as they are not given to employees but are earned by them. Under the Sales Tax Act, a sale of prepared food for immediate consumption is taxable.
- The tax base is determined by the cost of the food plus the cost of direct labor.
- When employees are required to purchase the meal, the tax base is the amount paid, even if it is a nominal amount.

Effective October 1, 2001:

- Meals provided to employees during work hours for free or at a reduced rate, to employees of food service establishments licensed by the Michigan Department of Agriculture, are not subject to sales tax.

FREE MEALS (not to employees)

- The Use Tax Act states “the tax levied under this act shall not apply to food for human consumption”. Based on this, all food being given away or used, including groceries and prepared food for immediate consumption, is exempt under the Use Tax Act. This is because the act has no provision for use tax on food. (MCL 205.94d)

VENDING MACHINE / MOBILE FACILITY

The statute was revised effective 01/01/95 stating, “Carbonated beverages sold from a mobile facility or vending machine, or food or drink heated or cooled mechanically, electrically or by other artificial means to an average temperature above 75° Fahrenheit or below 65° Fahrenheit before sale are taxable.... except milk, **non-carbonated beverages containing 10% or more juice content**, and fresh fruit.”

The calculation to determine tax due through a vending machine selling both taxable and exempt items was also revised. At the discretion of the taxpayer, it is either the actual gross proceeds from sales at retail, or 45% of the items subject to and exempt from tax, not including the sales of carbonated beverages.

The statute was again revised effective 01/01/01 stating in part that sales tax applies to food or drink heated or cooled mechanically, electrically, or by any other means to an average temperature above 75° Fahrenheit or below 65° Fahrenheit before sale, except milk, **non-alcoholic beverages in a sealed container (e.g. pop, juice products, water, etc.)** and fresh fruit.

References: MCL 205.54g
MCL 205.94d(3)
R 205.74
R 205.136

RAB 88-42
RAB 91-18
RAB 91-19
LR 75-4

HEARING AIDS, CONTACT LENSES, EYEGLASSES, AND EQUIPMENT TO SUBSTITUTE FOR PART OF THE HUMAN BODY TO ASSIST THE DISABLED

The following items are exempt from tax if purchased on a written prescription or order issued by a health professional:

- 1) Hearing aids
- 2) Contact lenses (if prescribed for a specific disease that precludes the use of eyeglasses)
- 3) Other apparatus, device or equipment used to replace, substitute, support, or supplement a part of the human body
- 4) Equipment used to assist the disabled person to lead a reasonably normal life

Repair and replacement parts for the above items are also exempt.

A “**health professional**” means a physician, dentist, optometrist or any other individual licensed, certified, or authorized by the director of the Department of Public Health to practice that specific profession.

Exempt prescription sales **must** be supported by **all** of the following:

- Record showing the date the prescription was issued
- Name of the person issuing the prescription
- Name of the individual for whose consumption it was issued
- Brief description of the property sold
- Amount charged to the customer

The original prescription should be attached to the seller’s copy of the sales invoice as proof of its authenticity and exemption.

Examples of items that may qualify as exempt if sold pursuant to a written prescription or order:

- Artificial eyes, limbs
- Braces
- Canes
- Corrective shoes
- Crutches
- Eyeglasses
- Hydraulic lift (patient lift for vehicles and homes)
- Hypodermic syringes and needles
- Oxygen equipment
- Pacemakers
- Specially built hospital beds
- Trusses
- Walkers
- Wheelchairs

The sales of **nonprescription** apparatus, devices or equipment and their repair and replacement parts are **taxable**.

MEDICARE AND MEDICAID PURCHASES

Medicare is a medical insurance program covering certain health services and drugs obtained by the insured with the cost of the program being shared equally between the Federal Government and the individual. The supplier sells tangible property or services directly to the person insured. Sales, other than prescription items, made to persons covered by Medicare are subject to tax.

Medicaid is a medical assistance program administered by the Family Independence Agency (FIA) for the medically indigent. Sales of tangible property or services are made **directly to** the FIA or there is a contract arrangement with a fiscal agent. Payment is made directly from state funds for Medicaid sales and are therefore exempt.

References: MCL 205.54a(1)(h)

MCL 205.94(1)(p)

LR 78-8

LR 87-46

LR 87-51

LR 87-52

LR 2002-01

LR 2002-02

HOUSE RENTALS

The receipts from lodging are generally taxable except the receipts for rooms and lodging rented for a continuous period of more than 30 days to the same person. Lodging is defined in the statute as rooms or lodging furnished by hotelkeepers, motel operators, and other persons furnishing accommodations that are available to the public on the basis of a

commercial and business enterprise. Included in the meaning of hotel and motel are:

- Inns
- Motels
- Cottages
- Tourist homes
- Tourist houses or courts
- Lodging houses
- Rooming houses
- Nudist camps
- Apartment hotels
- Resort lodges and cabins
- Camps operated by other than nonprofit corporations where a structure is rented
- Any other building or group of buildings in which accommodations are available to the public

Not included in the meaning are childcare facilities licensed under Act 116 of the Public Acts of 1973.

For purposes of this topic, business is defined as an activity engaged in by a person with the object of gain, benefit or advantage, either direct or indirect.

References: MCL 205.92(h)
MCL 205.93a(b)
R 205.88
RAB 90-31
LR 71-03
LR 86-06

LR 87-08
LR 89-03

INDUSTRIAL LAUNDRIES

Effective January 1, 1998 sales or leases of the following categories of products to industrial laundries are exempt from taxation:

- Textiles and disposable products, e.g. soap, paper, chemicals, tissue, deodorizer and dispensers, packaging, supplies, hangers and name tags
- Equipment used to repair and dispense textiles
- Machinery, equipment, parts, lubricants and repair services used to clean, process and package textiles and related items
- Various utilities
- Production washroom equipment and mending/packaging supplies and equipment
- Material handling equipment
- Wastewater pretreatment equipment, supplies and related maintenance and repair services

After December 31, 1998, the laundering or cleaning of textiles under a sale, rental, or service agreement with a term of at least 5 days is subject to use tax. Tax does not apply to the laundering or cleaning of textiles used by a restaurant or retail sales business.

“Restaurant” means a food service establishment defined and licensed under the Public Health Code.

References: MCL 205.54a(1)(n)
 MCL 205.92(n)
 MCL 205.93a(d)
 MCL 205.94 (1)(bb)

INTERSTATE COMMERCE

Interstate or foreign commerce means any activity between different states and countries. Sales where ownership transfers out of this state are not subject to Michigan's sales tax as these transactions involve interstate commerce activities that are prohibited by constitutional laws of the United States. Intrastate transactions or those transactions in which tangible personal property is located within the state at the time of sale and is delivered within the state are subject to sales tax.

Determining which transactions are protected by the U.S. Constitution depends on the facts in **each individual case**.

To make a valid claim of deduction for interstate commerce, a seller must document **each shipment** outside the state. Acceptable documentation includes the following:

- A waybill or bill of lading
- An insurance or registry receipt issued by the U.S. Postal Service
- Original shipping documents

Examples of Interstate Commerce (IC) Transactions:

- Sales for delivery to the purchaser out of state: **IC, Exempt**
- Sales to a Michigan resident for delivery to himself outside the state: **IC, Exempt**
- The order is placed from and **delivery is made to** locations **outside** of this state. Title does not transfer in MI: **IC, Exempt**

An example of a transaction which is not interstate commerce:

- Sales for delivery to a third party out of state by an instate purchaser: **NOT IC, Taxable**
- Sales for delivery in the State of Michigan: **NOT IC, Taxable**

NOTE: IC claims may also apply on printed materials delivered by printers to Michigan servicers for ultimate delivery to outstate locations.

References: R 205.81
 R 205.91

INTERSTATE MOTOR CARRIERS

TREATMENT UNDER THE SALES TAX ACT PRIOR TO 05/01/99

The Sales Tax Act [MCL 205.54r(1)(a)] provided a partial deduction from otherwise taxable receipts if all of the following apply:

- 1) The sale is to an interstate motor carrier
- 2) The product sold is a qualified truck or qualified trailer
- 3) The sale was made between 1/01/97 and 4/30/99
- 4) The tangible personal property must be used in interstate commerce

Out-of-State Usage Percent - This percent is computed by dividing fleet mileage of qualified trucks outside of Michigan (numerator) by fleet mileage of qualified trucks everywhere (denominator). **Fleet mileage of qualified trucks and trailers used solely in intrastate commerce is not included in this formula.**

Deduction

The deduction claimed on the sales tax return of a Michigan retailer would be the product of the out-of-state usage percent times the selling price of the qualifying equipment.

TREATMENT UNDER THE SALES TAX ACT AFTER 04/30/99

Effective 05/01/99, sales of rolling stock are exempt from sales tax.

TREATMENT UNDER THE USE TAX ACT PRIOR TO 05/01/99

The Use Tax Act [MCL 205.94k(2)] provided for two separate and distinct exemptions from use tax (MCL 205.94k(2)). The amount of the exemption was dependent on whether the transaction for the purchase, rental or lease was consummated in Michigan or outside of this state.

Michigan Purchases, Rentals or Leases

In order for interstate motor carrier equipment to be **partially exempt** from tax, **all** of the following requirements must be met:

- 1) Qualified truck and/or trailer
- 2) Used in interstate commerce
- 3) Purchased by an interstate motor carrier
- 4) Purchased between 1/1/97 and 4/30/99

If all of the above requirements are met, the exempt amount for equipment purchased, rented, or leased in Michigan would be the out-of-state usage percent times the equipment cost. This would result in the same tax base as computed under the Sales Tax Act.

TREATMENT UNDER THE USE TAX ACT AFTER 04/30/99

Effective 05/01/99 – Purchases, rentals, or leases of rolling stock are exempt from use tax.

Out-of-State Purchases, Rentals or Leases

Interstate motor carrier equipment will be **100% exempt** from tax if **all three** of these requirements are met:

- 1) Equipment is rolling stock
- 2) Used in interstate commerce
- 3) Purchased, rented, or leased by an interstate motor carrier

Definitions of terms that are the same for both sales tax and use tax:

Interstate Motor Carrier - a person engaged in the business of carrying persons or property, other than themselves, their employees, or their own property for hire across state lines and whose fleet mileage was driven at least 10% outside of this state in the immediate preceding tax year. "Immediate preceding tax year" is defined as follows for purposes of this definition:

- 1) The state's fiscal year (10/01 - 9/30) or
- 2) Businesses recently formed must have 12 months activity. For the first year only, the department will not require the 12 months to match the state's fiscal year.

Qualified Truck - A commercial motor vehicle power unit that has two axles and a gross vehicle weight rating in excess of 10,000 pounds, or a commercial motor vehicle power unit that has three or more axles.

Qualified Trailer - A trailer designed to be drawn behind a qualified truck.

Rolling Stock - A qualified truck, a trailer designed to be drawn behind a qualified truck and parts affixed to either a qualified truck or a qualified trailer. "Parts" do not include fluids (i.e. oil, windshield solvents, etc.) and gases (i.e. freon), windshield solvent, etc.

NOTE: Prior to May 1, 1999, parts were only exempt when purchased outside of this state.

References: MCL 205.54r MCL 205.94k

ISOLATED / CASUAL TRANSACTIONS AND AUCTIONEERS

ISOLATED/CASUAL TRANSACTIONS

The definition of "sale at retail" does not include an isolated transaction by a person **not licensed or required to be licensed** under the Sales Tax Act. Since an isolated or casual transaction is not a retail sale, it is not subject to sales tax. An **isolated or casual transaction does not apply should a person be licensed or be required to be licensed under the Sales Tax Act.**

Isolated transactions are not directly defined in the statutes, rules, etc. Instead, isolated transactions have been identified as something other than "sales at retail". Sales made on a repeated or successive basis are not isolated.

AUCTIONS/AUCTIONEERS

Auctioneers conducting auctions will be liable for tax if:

- He/she actually owns the merchandise **or**
- The auction is conducted off the premises of the client

Clients will be liable for tax if:

- The auction is on premises of client and the auction is conducted on a repetitive basis or,
- The merchandise is considered an ordinary stock of goods, e.g., inventory items

Auctions are exempt as isolated transactions if **all** of the following occur:

- On the client's premises
- Not conducted on a repetitive basis
- Merchandise is not an ordinary stock of goods

If sales at an auction were considered isolated transactions, they would not be subject to sales tax. However, the purchasers would be subject to use tax on the acquisition amounts.

The tax status of specific types of auctions is listed below. Assume all types of auctions listed are conducted on the client's premises, and the client retains ownership of the goods being auctioned. The factors that determine whether the client is responsible for sales tax or the purchaser is responsible for use tax are:

- The type of "goods" sold
- "Repetitiveness"
- Whether the client has or should have a sales tax license.

Federal Bankruptcy Auctions

Appointed bankruptcy trustees conduct these auctions in the ordinary course of business. These auctions would be considered taxable. The bankruptcy trustee would be required to remit sales tax.

Municipal Surplus Equipment Auctions

These auctions are conducted in the ordinary course of business by the municipal entity. These auctions would be considered taxable. The municipality would be required to remit sales tax.

Industrial Processing Auctions

These auctions normally contain a mixture of items; some items are the ordinary goods sold in the normal course of business and some items are not. Goods that would ordinarily be sold in the normal course of business would be subject to sales tax. This would include goods sold which are not the normal stock of goods sold, but which are sold on a regular repeated basis. For example, a business that sells at auction excess office equipment once every two years or when volume warrants would be subject to sales tax on these sales.

Retail Store Inventory

Inventory is ordinarily sold in the normal course of business, and is subject to sales tax. The sales would be taxable provided the items sold are ordinarily of a taxable nature. For example, if the inventory of a grocery store is auctioned, food items would not be taxable, however items such as paper products would be taxable. The retailer would be required to remit sales tax.

Retail Store Equipment & Fixtures

These items are not normally considered to be goods sold in the normal course of the retailer's business. Sales made at these auctions would be subject to sales tax provided the retailer has a sales tax license or is required to be licensed.

Vehicles

Normally, vehicle auction sales for clients other than vehicle dealers are not considered goods sold in the normal course of the client's business activity, unless five or more are sold in a twelve-month period.

These auctions would not be subject to sales tax provided fewer than five have been sold by the client within twelve months. The count of five would include vehicles sold at the auction. The client would be required to remit sales tax. Vehicle transactions are virtually always taxable, and if the sale is not subject to tax at the auction, the purchaser must pay 6% use tax. The seller would be required to collect sales tax if the auction is a multiple client auction.

Construction Equipment Dealer Inventory

Inventory is ordinarily sold in the normal course of business, and is subject to sales tax. Sales of construction equipment are normally taxable, however sales for certain uses or to certain purchasers can be exempt.

Charity Auction of Donated Gifts

Auctions of donated gifts do not represent isolated transactions. The charity would be considered to be engaged in a fundraising business activity as the normal course of business regardless of the frequency of auctions. The charity would be required to remit sales tax on its return.

In those instances where the bid is substantially greater than the value of the article, the department will apply the real object test. (Refer to RAB 95-1 for detailed information on the “real object test”.) Consequently, the tax base will either be the bid amount or the transaction will not be taxed because it will be viewed as a service.

Wholesaler or Distributor of Industrial Machinery or Retail Equipment

These items are ordinarily sold in the normal course of business and are subject to sales tax. Sales of industrial machinery can quite often be taxable, however sales for certain uses or to certain purchasers may be exempt.

Real Estate

Sales tax is imposed upon transactions involving tangible personal property, not real property. Sales of real estate are not subject to sales tax. However, an item normally considered real estate can become tangible personal property when sold. For example, a farmer sells his barn with the condition that it be dismantled and removed from the land. This represents tangible personal property in the form of wood representing a barn structure without the accompanying rights to the land upon which the barn sits.

Likewise, the sale of a house with the condition that it be removed from the land upon which it sits represents a sale of tangible personal property for the same reasons.

If the client makes regular repeated sales of this nature, the client would be required to remit sales tax when tangible personal property is being sold.

Construction Contractors Machinery

These items would not ordinarily be sold in the contractor’s normal course of business. These auctions would not be taxable, unless the contractor is in the business of selling machinery, or sells his machinery on a regular repeated basis. Transactions would be taxable should the contractor have a sales tax license or be required to have a sales tax license.

Rental Equipment Company Inventory

This inventory would fall within the definition of ordinary goods sold (rented) in the normal course of the client’s business. The auction of this inventory would represent taxable sales. The rental equipment company would be required to remit sales tax on its return.

References: MCL 205.51(1)(g)
MCL 205.94g
R 205.13
R 205.53
RAB 95-1

LR 72-08
LR 77-02
LR 79-01
LR 85-07
LR 86-30

Terco, Inc. v Michigan Department of Treasury, (1983) 339 N.W.2d 17, 127 Mich.App. 220

NEWSPAPERS, PERIODICALS AND OTHER PUBLICATIONS

RECEIPTS FROM THE SALE OF NEWSPAPERS, PERIODICALS, AND OTHER PUBLICATIONS

Sales tax generally does not apply to receipts from sales of newspapers, periodicals and other publications. To be exempt, one of these three conditions must be met:

- 1) Admitted under federal postal laws and regulations effective 9/01/85 as:
 - Second class mail matter (now designated as a “periodical”)
 - Controlled circulation publication (now called “requestor publications”)
- 2) Qualified to accept legal notices for publication in this state
- 3) Any other newspaper or periodical meeting **all** of the following criteria:
 - General circulation
 - Established at least 2 years
 - Published not less than once per week

The identification statement “Periodicals postage paid” will appear in the qualifying publication. It can be found on one of the first five pages, which may exclude advertising pages, or on one of the last three editorial pages inside the back cover.

Tangible personal property used or consumed in the production of newspapers, periodicals, and other publications may or may not be taxable. If the tangible personal property becomes a component part of the newspaper, periodical, or other qualifying publication it is exempt from taxation. Should the tangible personal property be used or consumed in the production process, but not become a component part of the newspaper, periodical, or other publication it is:

- Taxable if the newspaper, periodical, or publication is published more than 14 times per year.
- Exempt if they are published 14 times or less per year.

Newspaper Supplements

The definition of a newspaper supplement is a separate advertising supplement that is distributed with a newspaper or periodical. It includes political pamphlets, grocery coupons, clothing store ads, etc. Tangible personal property that becomes a component part of the advertising supplement is not taxable if:

- 1) The supplement is inserted **into** and circulated **with** a newspaper, periodical, or other publication that is exempt from tax.
- 2) It is delivered directly to the newspaper or periodical company by a person other than the advertiser or
- 3) The supplement is printed by the newspaper or periodical company.

RAB 88-33

LR 80-06
LR 87-36

LR 87-24

NONPROFIT ORGANIZATIONS

PURCHASES (by Nonprofit Organizations)

Sales and use tax exemptions are limited to those organizations that have federal tax-exempt status under sections 501(c)(3) or 501(c)(4) of the IRC, unless the organization was reissued an exemption ruling letter after June 12, 1994, by the Michigan Treasury Sales and Use Tax Division.

To be exempt, the property purchased must be used or consumed primarily in carrying out the purposes of the institution or agency, as stated in the bylaws or articles of incorporation of the exempt entity. Fundraising is not the stated purpose of an organization, even if the bylaws allow for such activities. Therefore,

purchases of property used in fundraising activities are taxable.

For all purchases to be exempt, the payment for the purchase must come directly from the funds of the exempt nonprofit organization. If the organization is selling the items to the members, at cost or above cost, the purchase is not exempt, unless a valid resale exemption applies.

In order to receive the exemption, the following **must** be provided:

- Exemption ruling letter reissued after June 12, 1994 by the Sales and Use Tax Division **AND** a Certificate of Exemption, claiming as the valid reason, “For use or consumption in connection with the operation of a nonprofit organization”.
- or
- Certificate of Exemption, claiming as the valid reason, “For use or consumption in connection with the operation of a nonprofit organization” **AND** a copy of the Federal exemption letter indicating the exempt status received from the Internal Revenue Service.

SALES (by Nonprofit Organizations)

The statute provides an exclusion for organizations that qualify for either of the above exemptions. These organizations may exclude, from gross proceeds, sales at retail that are less than \$5,000 for the calendar year. Nonprofit organizations making retail sales are still required to register and obtain a sales tax license even if their total sales are below the limit. If the total sales at retail are \$5,000 or greater, tax is due on the entire amount. Sales tax billed separately must be remitted regardless of the \$5,000 exclusion, pursuant to the enrichment provisions.

References: MCL 205.54a(1)(a)
MCL 205.94(1)(z)

RAB 95-3
RAB 96-6

LR 78-5

POLLUTION CONTROL FACILITIES, COMPONENT PARTS

The General Sales and Use Tax Acts allow a deduction or exemption for the sale or purchase of tangible personal property to be installed as a component part of a water or air pollution control facility. The deduction or exemption is dependent on a tax exemption certificate issued by the State Tax Commission. Issuance of a certificate is contingent upon satisfying the conditions found in the Natural Resources and Environmental Protection Act, Act No. 451 of the Public Acts of 1994.

The Sales and Use Tax Acts are interpreted in Rule 87 as follows:

- 1) Tangible personal property purchased for installation as a component part of an air or water pollution control facility for which the State Tax Commission issues a tax exemption certificate is exempt from tax.

- 2) When tax has been paid on tangible personal property which later qualifies for exemption as a result of obtaining a certificate of exemption from the State Tax Commission, a refund may be requested upon submission of both of the following documents to the Treasury department:
 - a) A copy of the exemption certificate issued, indicating the approved cost of the tangible personal property installed and entitled to exemption
 - b) A copy of the seller's invoice showing the name and address of seller, identification of the purchaser, identification of the items purchased, date of purchase, and amount of tax paid.

The entity that paid the tax to the Treasury department requests the refund. Their customer, who provides a copy of the Pollution Control Exemption Certificate and asks for their tax to be refunded, prompts the request.

To facilitate the refund process, the owner of the pollution control facility can provide the department's Technical Services Division with a copy of the Pollution Control Exemption Certificate, together with a list of vendor invoices qualifying for the sales tax credit. That division will respond with their approval or disapproval to facilitate the refund process through the vendor.

The certificate describes the property that qualifies for tax exemption. It includes items that become part of real property. The flow through exemption applies when the contractor purchases exempt personal property for these pollution control projects.

Summary

- An entity must apply for and be granted a pollution control exemption certificate by the Michigan State Tax Commission before any of its purchases qualify for this exemption.
- The certificate will state the total cost of the property entitled to exemption. The final cost of material in the pollution control facility may exceed this amount. Amounts exceeding this limitation are subject to tax.
- Equipment benefiting the business or personnel will be taxable. Examples would include but are not limited to heat recovery equipment, air make-up units, equipment used to prepare and return contaminants to the process, etc.
- Replacement equipment and repair parts acquired in subsequent years may be taxable items if their additional costs would cause the project to exceed the stated exempt value in the original exemption certificate.
- The utility costs associated with the operation of these facilities do not qualify for the exemption given to the facilities.
- The effective date of the certificate is its date of issue.
- It continues in force until it is revoked or the facility is no longer used for its primary purpose.

If the State Tax Commission, through a pollution control exemption certificate, states that certain property is exempt from sales and use taxes, it is exempt.

References: MCL 205.54(1)(l)
MCL 205.94 (s)
R 205.137
RAB 90-2

PRESCRIPTION DRUGS

Sales or purchases of prescription drugs for human use are not subject to tax.

“Prescription drugs for human use” includes:

- Insulin
- Drugs whose nature is that they can only be dispensed by a licensed pharmacist
- Oxygen dispensed pursuant to a written prescription or order issued by a licensed physician or other health professional as defined in PA 368 of 1978.

As a general rule, if you can purchase the identical drug at any time over the counter, it does not qualify for the exclusion.

Syntex Laboratories v Department of Treasury, 18 Mich App 383; 470 NW2d 665 (1991) determined that the samples of drugs given out by a manufacturer to physicians, then dispensed as free samples to patients were not taxable because their nature was that they could only be dispensed legally by a licensed pharmacist or health professional. However, any packaging or container that comes with the sample drug is taxable.

References: MCL 205.54g
MCL 205.94d
RAB 93-3

Syntex Laboratories v Michigan Department of Treasury

PROMOTIONAL PRODUCTS

Promotional merchandise and packaging material acquired for use in fulfilling a redemption offer or rebate to a person located outside this state are exempt.

Reference: MCL 205.94 (1)(c)

PURCHASE OF BUSINESS

Although isolated/casual transactions are not subject to sales tax, there are no provisions in the Use Tax Act to exempt them. However, the Use Tax Act provides an exemption for property purchased from a seller if the property is part of the purchase or transfer of a business. A purchase or transfer of a business takes place if 1 or more of the following occurs:

- Acquirer intends to use the seller's trade name or goodwill.
- Acquirer intends to continue all or part of the seller's business.
- 75% of the seller's tangible personal property is acquired at 1 or more of the existing locations.

The exemption **does not** apply to:

- Property that would be sold in the ordinary course of a trade or business (inventory items)
- Motor vehicles, ORVs, mobile homes, aircraft, snowmobiles or watercraft

Reference: MCL 205.94g

RAILROADS

Generally, any equipment, accessories, parts, materials for repair, and supplies used in rail operations are exempt. The exemption does not apply to vehicles licensed and titled for use on public highways.

References: MCL 205.54m
 MCL 205.94(*l*)

RENAISSANCE and ENTERPRISE ZONES

RENAISSANCE ZONES:

Sales and use taxes were not abated when the Renaissance Zones were created. A company or an individual residing within a Renaissance Zone has no special exemption from sales or use taxes.

ENTERPRISE ZONE:

Benton Harbor is Michigan's only Enterprise Zone (EZ).

The General Sales and Use Tax Acts granted exemption for a sale or purchase of tangible personal property for use in a qualified business activity of the purchaser. "Qualified business activity" is:

- 1) the activity of a qualified new business
- 2) the activity of an existing business that is attributable to a new facility.

Unless the certification of a qualified business is revoked as provided in the EZ Act, the exemption, credit or deduction granted to it continues for ten years from the date it was certified. The last firms that were certified as qualified businesses will lose their exemption status in 2006.

To summarize, the sales and use tax deductions or exemptions are available to Enterprise Zone companies only if the following conditions are met:

- 1) The purchaser or consumer was certified as a "qualified business" by the EZ Authority at the time of the sale.
- 2) The personal property purchased by or leased to a "qualified business" was not acquired for resale or resale leasing.
- 3) The personal property acquired was to be used within the EZ or its exemption had to be proportionally reduced using traditional auditing procedures.

The General Sales Tax Act exempts property used in a qualified business activity. **The exemptions do not apply to services taxed under the Use Tax Act.**

References: MCL 205.54j
MCL 205.94h
RAB 93-10

SCHOOLS, HOSPITALS AND CERTAIN NONPROFIT INSTITUTIONS

Gross proceeds used for the computation of sales or use taxes generally need not include sales not for resale of tangible personal property to schools, hospitals, or certain nonprofit institutions. This deduction is not limited to institutions incorporated or domiciled in Michigan. For example, title to personal property can transfer to an out-of-state nonprofit hospital in Michigan and the sale can be exempt from sales tax.

The exclusion also applies to homes for the care of children or aged persons which are operated either by an entity of government, a church, a religious or fraternal organization, a veteran's organization, or a corporation incorporated under the laws of the state.

All of the above entities must have nonprofit status and meet the various qualifications and restrictions mentioned below before a deduction can be allowed. Acceptable exemption claims supporting tax exempt sales are discussed in the "Exemptions and Requirements" section of this text.

SCHOOLS

A school, as defined in the Administrative Rules, is an educational institution or an institution of learning. It must be operated by an entity of government, a church or a religious or fraternal organization and be organized solely for educational purposes. It has to maintain a faculty of qualified instructors, and teach regular, continuous courses of study, and confer upon students a recognized diploma or certificate upon completion of a specific curriculum.

Public and nonprofit private schools, charter schools and colleges may qualify. Public schools could be operated, for example, by the state of Indiana and be exempt from sales taxes when purchasing in Michigan.

Purchases made by nonprofit schools are exempt **if** payment moves from the funds of the school **and** the item(s) acquired is (are) to be used or consumed in connection with the operation or purpose of the institution.

A sale of tangible personal property to a parent cooperative preschool is exempt from taxation under both the General Sales and Use Tax Acts. The definition of a "parent cooperative preschool" taken from the General Sales Tax Act is as follows:

"... "Parent cooperative preschool" means a nonprofit, nondiscriminatory educational institution, maintained as a community service, and administered by parents of children currently enrolled in the preschool, that provides an educational and developmental program for children younger than compulsory school age, that provides an educational program for parents, including active participation with children in preschool activities, that is directed by qualified preschool personnel, and that is licensed by the Department of Consumer and Industry Services pursuant to Act No. 116 of the Public Acts of 1973, being sections 722.111 to 722.128 of the Michigan Compiled Laws".

Example: A parent cooperative preschool incorporated in **Indiana**, purchased playground equipment from a Michigan manufacturer in Kalamazoo. To save some money, a few parents volunteer to pick up the equipment and transfer it to Indiana. Because the exemption is limited to institutions that are licensed by **Michigan's** Department of Consumers and Industry Services, this "parent cooperative preschool" is not exempt under the school deduction.

Statute exempts from gross proceeds sales for fund raising purposes made by certain organizations, if their total calendar year sales at retail are less than \$5,000 and the sales tax was not collected as a separate item. "School" is defined in the act in such a way as to allow a separate exemption to the elementary, middle, junior or high school sites.

"Total calendar year sales at retail" includes all sales other than for resale or for lease. Examples of these sales at retail would be exempt meals and textbooks sold to students, meals sold to teachers, and fund-raising items sold to the public.

Examples of Exempt Sales:

- Sales made by a nonprofit educational institution of food to its enrolled students
- **Textbooks** sold by public or nonpublic schools to their enrolled students in kindergarten through the twelfth grade
- Athletic equipment sold to an educational institution for consumption or use (The athletic activities are under the management and control of the educational institution and the entire receipts are expended for athletic or educational purposes.) (R 205.74)
- Printing materials sold to a school for use by the student government, school newspaper and school magazine, if the items were purchased on a nonprofit school's purchase order using general funds.
- Building materials sold to a school for use in their building trades curriculum (The materials are used by the students to build homes that are sold upon completion.)
- A manufacturer and seller of jackets sells its wares to a school after accepting an exemption claim in good faith. The seller did not know that the jackets would later be sold to student groups, booster clubs, and PTA groups or that these groups were unlicensed. The school would be liable for the sales tax on their sales of these jackets assuming their total calendar year sales at retail met or exceeded \$5,000.

Examples of Taxable Sales:

- Food sold to teachers or visitors by schools or educational institutions
- Food sold by a state college to students attending a high school prom
- Fund-raising items sold to a nonprofit school without accepting a claim in good faith.
- Sales of class pins, rings, and similar articles when paid for, directly or indirectly, by the students (R 205.74)
- Sales to educational associations, parent teacher organizations, teachers, and other personnel of an educational institution (R 205.74)

HOSPITALS

The term “hospital” is not defined in the Sales and Use Tax Statutes. It is, however, defined in R 205.87 as follows:

“A “hospital”, for the purpose of this rule, means only a separately organized institution or establishment, the primary purpose of which is to provide medical, obstetrical, psychiatric or surgical attention **and** nursing to persons requiring the same.”

This definition is intended to serve an identification function when dealing with purchases of tangible personal property by and sales to nonprofit hospitals.

For Sales and Use tax purposes, the Department will use the above description to identify a “hospital”. It is the only definition of a hospital available when determining if the purchase is by or the sale is to a nonprofit hospital.

NOTE: A different definition of “hospital” is used for purposes of the contractor flow through exemption. See the “Contractor” section of this text.

In addition to the nonprofit requirement, the qualifications stated below must be met to qualify for any exemption:

- The entity must be a hospital. Parent holding companies, brother/sister or subsidiary property companies are not entitled to the exemption.
- The “medical, obstetrical, psychiatric, or surgical attention” must be of an acute nature and required in treating the illness, injury, disease or other similar medical condition. **Usually** this treatment would require the daily supervision of a physician and admittance to the hospital of **all** patients. A few individuals receiving acute care in a nursing facility setting would not qualify the facility for the hospital exemption.
- Nursing **must** be provided but it cannot be the primary function of the facility.

Only a hospital can lawfully use the word “hospital” in its name. However, a veterinary hospital may use the word and not qualify for the exemption. The lack of state or federal government accreditation may suggest that an entity is not a hospital. Not all hospitals (e.g., VA hospitals) are required to be accredited.

Sales by hospitals:

Sales by hospitals which are taxable retail sales include, but are not limited to, the following:

- 1) Meals sold to visitors and employees (R 205.87)
- 2) Nonprescription drugs, nonprescription medicines, and supplies sold to the public through the hospital pharmacy (R 205.87)
- 3) Sales of cosmetics, souvenirs and other similar merchandise (R 205.87)
- 4) Equipment sales to doctors or professional corporations. Hospitals sometimes use their purchasing power to acquire items at prices below those available to a colleague associated with the hospital.

- 5) Utility sales where the hospital is prorating its tax exempt utility bills among its lessees of office space

Retail sales by hospitals that are not taxable include, but are not limited to, the following:

- 1) Drugs, medicines, insulin, meals, and other miscellaneous items furnished to patients and consumed on the premises (R 205.87)
- 2) Charges for oxygen, blood plasma, and blood administered to patients (R 205.87)
- 3) Dressings and bandages applied in the hospital (R 205.87)
- 4) Charges for X-ray radiation treatments, braces, splints, cases, therapeutic diets, and intravenous solutions furnished patients (R 205.87)
- 5) Charges for anesthesia supplies and laboratory tests (R 205.87)
- 6) Sales of eyeglasses prescribed or dispensed to correct a person's vision by an ophthalmologist, optometrist, or optician, and repair and replacement parts for such eyeglasses (R 205.104)

OTHER TYPES OF NONPROFIT INSTITUTIONS

Churches, schools and governmental agencies are nonprofit entities that are discussed elsewhere in this manual. This section addresses other nonprofit institutions that are limited to homes for the care and maintenance of children or aged persons. To qualify for the exemptions found in the Sales and Use Tax Acts, the following conditions have to exist:

- The home must be operated by an entity of government, a regularly organized church, religious or fraternal organization, a veteran's organization, or a corporation incorporated under the laws of the state (Michigan). The home does not have to be separately incorporated.
- The home cannot be operated for profit, which means that the income does not inure, in whole or in part, to an individual or private shareholder.
- The activities of the home are carried on exclusively for the benefit of the public at large and are not limited to the advantage, interests and benefits of its members or a restricted group.

Purchases are still not automatically exempt from tax. Items sold to or acquired by these homes have to be consumed and not resold. In addition, the sales tax exemption requires that the transferee sign a statement, approved by the Department, stating that the property is to be used or consumed in connection with the operation of the institution or agency and that it qualifies as exempt under the statute.

References: MCL 205.54a(a)	R 205.74	RAB 95-3
MCL 205.54q	R 205.87	RAB 96-6
MCL 205.94(h)	R 205.104	LR 73-4

VEHICLES

The General Sales Tax Act provides the following exemptions for sales of vehicles when specific criteria are met.

A sale at retail does not include vehicles acquired for demonstration purposes by a new car or truck dealer. The exemption is determined by the number of new cars and trucks sold during a calendar year without regard to the specific make or style in accordance with the following schedule [MCL 205.51(b)]:

- 0 to 25 units sold = 2 exempt demonstrators
- 26 to 100 units sold = 7 exempt demonstrators
- 101 to 500 units sold = 20 exempt demonstrators
- 501 or more units sold = 25 exempt demonstrators

If a non-resident is issued a special registration (in-transit permit) for the purchase of a vehicle to be titled and registered in his/her home state, the Michigan sales tax cannot exceed the sales tax that would have been charged by the other state (MCL 205.52a). Non-reciprocal states are exempt from Michigan's sales tax with the special registration. In computing the tax due in the non-resident's home state, trade-ins, if applicable, are not part of the tax base.

The dealer must obtain a certificate from the purchaser and furnish the Department the following information:

- Name
- Address
- Signature
- Statement that the vehicle shall be primarily used, stored, and registered outside of Michigan
- Jurisdiction of registration

The information can be provided by way of certification on the RD-108, Application for Title and Registration form, that is completed at the dealership.

A sale of a vehicle in interstate or foreign commerce is exempt if the following conditions are met (R 205.54):

- The dealer must not have knowledge that the vehicle will be returned to Michigan
- Vehicle ownership passes outside the state
- A Michigan title and license are not required
- The dealer maintains records to substantiate the above facts

Ambulances and fire department vehicles are exempt from taxation if [MCL 205.54a(i)]:

- The vehicle is not for resale.
- The purchaser is a Michigan nonprofit corporation organized exclusively to provide a community with ambulance and/or fire department services.

NOTE: The Federal government and the State of Michigan and its local governmental entities are exempt from tax, therefore any ambulance or fire department vehicle purchased by them is exempt.

A vehicle sold to a nonresident military personnel for registration in his/her home state is exempt from Michigan Sales Tax at the time the vehicle is sold. The

immediate commanding officer must issue a sworn statement certifying active duty status and the home address of the purchaser (MCL 205.54e).

After April 30, 1999 the sale, rental, or lease of rolling stock to an interstate motor carrier, that is used in interstate commerce, is exempt from taxation (MCL 205.54r). See the “Interstate Motor Carriers” section in this text.

A vehicle brought into Michigan within 90 days of purchase from outside of the state is presumed to be subject to tax. The burden of proof of exemption rests with the purchaser. This presumption does **not** mean items brought into Michigan on the 91st day or thereafter are not subject to tax if the intent was to bring the item(s) into Michigan.

MCL 205.93, Section 3(2) states that tax must be collected by the designated state department before the transfer of title of vehicles, ORVs, mobile homes, aircraft, snowmobiles or watercraft unless the purchaser is a licensed dealer or retailer purchasing for resale.

Taxable price is not less than retail market value.

The following purchases or transfers are not subject to Use Tax:

- Among and between the following specific relatives:

Spouse	
Mother or step-mother	Father or step-father
Brother or step-brother	Sister or step-sister
Child	Step-child
Grandparent	Grandchild
Legal ward	Legally appointed guardian with a certified letter of guardianship
- A gift received as a beneficiary in the administration of an estate
- As part of a(n) organization, reorganization, partial liquidation or dissolution of a business, provided specific criteria are met (RAB 91-1)
- Distressed vehicles acquired by an insurance company

The Treasury Department may request and use information from any other state agency in order to verify vehicle exemption or questionable valuation claims.

References:	MCL 205.51(b)	R 205.54	RAB 91-1
	MCL 205.52a	R 205.135	RAB 98-4
	MCL 205.54a		
	MCL 205.54e		
	MCL 205.54r		
	MCL 205.93		

VESSELS

Both the General Sales Tax and Use Tax Acts provide for the exemption of certain commercial (water) vessels.

- Specially ordered (or self manufactured) water vessels over 500 tons are exempt. All supplies for those water vessels are also exempt if used in interstate commerce, but taxable if used in foreign commerce.
- All other vessels are taxable

Fuel and supplies for use on pleasure craft are subject to tax. Public Act 519 of 1988, exempts vessels and supplies used in commercial fishing (not charter fishing).

Prepared food sold for resale to vessel operators is exempt if the final retail sale of the food within Michigan waters is taxed.

References: MCL 205.54a(1)(d)
 MCL 205.94(1)(j)
 R 205.131